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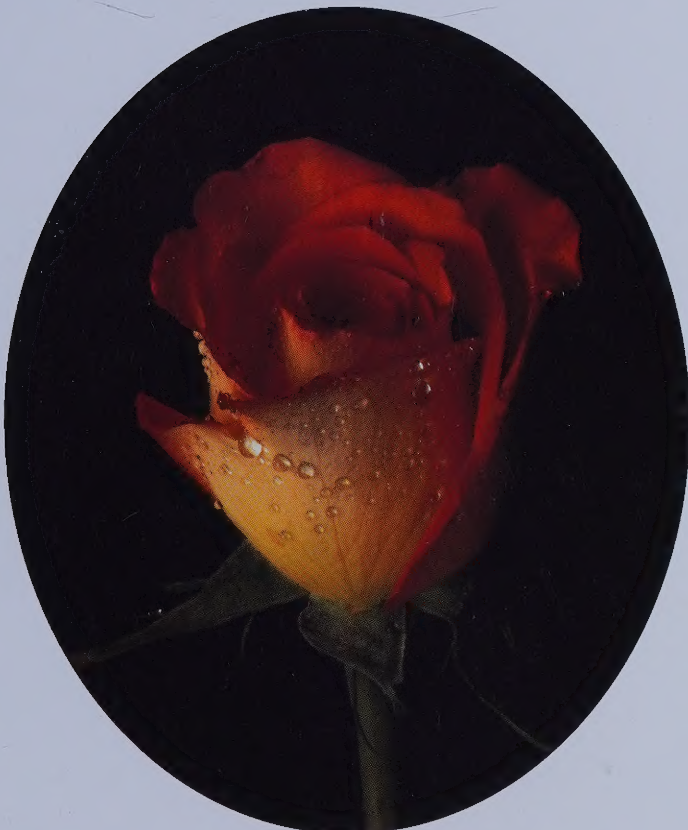
Enscor Inc.



Annual Report 1997

ENSCOR INC.
ANNUAL REPORT
1997

TABLE OF CONTENTS

Note on Currency: In this Annual Report, unless otherwise specified or the context otherwise requires, all dollar amounts are expressed in United States dollars.

About the Cover

Reminiscent of our Company's historical involvement in the real estate industry through The Rose Corporation and in anticipation of our proposed name change, we have chosen the image of a rose to herald the return to our roots described elsewhere in this Report.

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Enscor Inc.'s Canadian operations are currently focused on both long and short-term real estate investment activities. Short-term investments consist of mezzanine financing, equity loans, bridge loans, and other forms of credit enhancement to development projects being managed by others. The balance of our activity will involve the acquisition and management of niche income producing properties, such as assisted care adult living centres, self-storage mini-warehouse facilities, and hotels.

The Company's U.S. operations continue in a limited way in the heat exchange industry through its ownership of California based Hayden Industrial Products. Hayden manufactures and markets heat exchangers for industrial and mobile applications and for heavy-duty trucks.

LETTER TO SHAREHOLDERS

At the end of last year's Letter to Shareholders, having concluded the sale of most of the components of The Equion Corporation and being down to our last remaining land holding in Whitby, Ontario, we recognised a need for a future business strategy for Enscor that would earn the confidence and support of our shareholders. Since then, we have completed the sale of all of the remaining Equion businesses, except for the Hayden Industrial Division, and have concluded the sale of our land in Whitby. As a result of this activity, our balance sheet at year end reflected a manufacturing concern in southern California, a successful resort hotel in northern Ontario, and a considerable pool of cash and near cash assets. Although the Business Review section of this report discusses our activities over the past year, the bulk of this letter will address our plans for the future. We hope that you will share our sense of excitement and enthusiasm for our new direction which, as you will soon see, is really a return to our roots.

Over the past year, we have actively explored a new real estate investment direction for Enscor, a direction recently endorsed by your Board of Directors, and a direction which will exploit the core competencies acquired by senior management over many years. Our strategy for income generation and wealth creation will employ both short and longer-term components. A portion of our portfolio will take the form of short-term investments in active development projects. These investments are expected to generate high rates of return and may create opportunities for more permanent investment. We intend to invest the balance, and indeed the majority, of our capital in specialised income producing and growth oriented real estate assets.

The short-term side of the business may best be thought of as structured real estate financing. We offer financial support to experienced real estate developers in need of equity or near equity loans to enable them to source traditional construction and take-out financing from banks, trust, and insurance companies. Our participation may take the form of a direct equity investment, a mezzanine loan, a very short-term bridge loan, a pre-purchase of inventory or, in some cases, a guaranty or other credit enhancement device. We tailor our participation and the terms of each financing to the particulars of the project, the nature and extent of the client's commitment, the demands of the traditional lenders, the alternate security available, and the preferences of the client.

Our own background in the real estate development business permits us to quickly and capably assess opportunities in light of current market conditions, and to add value to our client's project through advice and sometimes direct intervention. Having been there ourselves, we understand the vagaries of the business and are able to adapt and adjust our participation and financial support to meet circumstances as they unfold. Our clientele values our responsiveness, our expertise, and our flexibility as the factors that separate us from more traditional lenders. Regardless of our role, we take an active interest in each project funded and do not consider our involvement successful unless our client's financial objectives are also met. Investments in this portfolio are expected to show returns in the range of 25 to 40% or higher per annum and are generally designed to be outstanding for between not less than six and not more than thirty months. To facilitate our participation in a greater number of projects, we have established informal alliances with others engaged in related activities.

The second leg of our strategy reflects our appreciation of the fact that the investment quality of any asset, including real estate, is only as good as the management expertise that can be applied to it. In light of this, we will engage in the direct acquisition of income producing real estate assets connected with several core business areas and will align ourselves with a small group of entrepreneurs, each of whom has a demonstrated ability to manage and develop properties within their respective niches. The business areas under active consideration include assisted care adult living centres, self-storage mini-warehouse facilities, and hotels. This strategy is predicated on the belief that each area of endeavour will prosper best if the individual talents of those who will be managing it are allowed to operate in the independent entrepreneurial environment in which they have succeeded. In each case, we will supply

most or all of the capital to acquire the assets. While arrangements may vary over time, our management partners will, through their own companies, enjoy minority participation in the cash flow and value growth of the assets, as part of their reward for originating and managing the investments. We also intend to acquire a significant direct ownership interest in each of those management entities.

The adoption of this business strategy has a number of implications. Although we have amassed significant equity, much of which is quite liquid, we will require additional funding to meet our objectives. To this end, we have commenced two discreet initiatives. First, we have announced our intention to sell Hayden Industrial Products to an entity controlled by Enscor's principal shareholder group. The transaction and the ascribed value will be supervised by an independent committee of the Board pursuant to the appropriate regulatory guidelines. This initiative has a dual motivation. Most directly, it will see the injection of cash above book value. At least as important, however, it will render Enscor a pure real estate investment vehicle going forward, which is critical to the second motivation, the need to raise additional capital. We are currently exploring various financing options.

With the exception of a small private placement of debt and preference shares in 1988, Enscor has not raised money in the capital markets since the time of its initial public offering. We sit today with common equity of approximately $25 million and no debt. We now have a plan which generates a clearly defined need for additional capital. While the short-term side of our investment activity can be supported, for the time being, by our existing resources, and is expected to generate substantial profits, our long-term investment strategy requires a major commitment of capital.

In light of this, and so as to establish an acceptable valuation of the Company for financing purposes, we will make a concerted effort to develop a more meaningful following for the Company and its stock, including initiatives to help get and keep the message out in the investment community. We also intend to expand and modify our Board from its existing seven directors, to nine individuals chosen, in part, for their ability to assist us in implementing and advancing our strategy. Finally, at our upcoming Shareholder's Meeting, we will seek approval for a name change to The Rose Corporation, reflecting our active return to the real estate environment. We believe that the marketplace will respond positively to these initiatives.

We are enthusiastic about our new direction. It manifests a decision to actively exploit clearly defined areas of competency, knowledge, and experience within our senior management group in a very focused way. We believe that this return to our roots will bear fruit for many years to come.

Yours very truly,

SAM REISMAN
Chairman and Chief Executive Officer

STEPHEN R. MORRISON
President

BUSINESS REVIEW

Overview

Enscor's U.S. operations are currently in the heat exchanger industry through Hayden Industrial Products LLC. Until December 1996, Hayden was a division of The Equion Corporation. Approximately 70% of Equion was acquired in May 1993, and the remainder during fiscal 1996. In addition to Hayden Industrial Products, Equion engaged in other manufacturing and distribution activities, primarily in the automotive industry. As described below, these other businesses have been sold.

In Canada, operations are now focused on real estate investment. There will be both short and long-term aspects to the business activities. The short-term side will consist of financing development projects carried out by others. The long-term strategy will be to invest in certain specialized income producing and growth oriented real estate assets.

Prior to 1993, the Company concentrated its active operations on real estate development within the Greater Metropolitan Toronto commutershed. Activities included development and sale of land, marketing and building of low and high-rise residential properties, and the development of commercial sites for retention or sale. The Company began an orderly withdrawal from the industry commencing in late 1991 and sold its last remaining active development site in 1997.

Automotive and Industrial

On July 31, 1995, Equion completed the sale of Signet Systems, one of its four U.S. divisions, together with Signet AutoAir, an 80% owned German subsidiary. Signet and Signet AutoAir manufactured climate control systems and components, primarily serving original equipment manufacturers. In the fall of 1995, stimulated by the express desire of its minority shareholders to have their shares repurchased, Equion initiated a process to sell its remaining aftermarket and industrial businesses.

During fiscal 1996, the TCI and Trans-Tool divisions were sold, along with Hayden's aftermarket engine driveline product line. TCI manufactured and marketed high-performance automotive products, while Trans-Tool manufactured and marketed specialty transmission repair tools and garage equipment. In December 1996, Equion completed the sale of Hayden's aftermarket cooling business. Subsequently, in an internal reorganization, Hayden's remaining industrial cooling products business was transferred to a separate wholly-owned entity, and Equion was liquidated into another Enscor subsidiary.

Cooling Systems

(Part of heat exchanger industry)

Hayden's industrial cooling products business, based in California, manufactures and markets heat exchangers for industrial and mobile applications and for the heavy-duty truck industry. In addition to oil coolers sold to OEMs in the truck sector, Hayden sells a broad line of heat exchangers and accessories to industrial OEMs and to fluid

power distributors. Most of Hayden's products are highly engineered, designed for specific applications, or in response to specific customer needs.

Real Estate Investment

During the year, the Company completed the sale of its Whitby site, representing the last remaining active development project, and refocussed on real estate investment. Previously active managers and operators of a real estate development and residential construction business, the Company will now concentrate on financing short-term development projects carried out by others and investing in certain niche long-term income producing real estate assets.

Short-term financing and development

Sometimes referred to as merchant banking, the short-term structured financing side of the business will take the form of direct equity loans, mezzanine loans, short-term bridge loans, a pre-purchase of inventory, or in some cases, nothing more than a guaranty or other credit enhancement device. Project terms will typically range between six and thirty months. These short-term high-yield investments are expected to provide a profitable earnings base and, more importantly, may lead to investment opportunities for our long-term business focus.

Customers are typically experienced real estate developers in need of equity or near equity loans to enable them to source traditional construction and take-out financing from banks, trust, and insurance companies.

Long-term income producing

The long-term focus will involve the acquisition of real estate assets connected with several core business areas. The business areas presently under consideration include assisted care adult living centres, self-storage mini-warehouse facilities, and hotels. Common to each is its real estate orientation, leading to an alignment with a small group of entrepreneurs, each of whom has a demonstrated ability to manage and develop properties within their niche. In each case, the Company will supply most or all of the capital to acquire the assets. While arrangements may vary over time, our management partners will, through their own companies, enjoy minority participation in the cash flow and value growth of the assets as part of their compensation for originating and managing the investments. It is also anticipated that the Company will acquire a substantial interest in each of those management entities.

As part of its long-term income producing business, the Company owns the Best Western Hidden Valley Resort Hotel in Huntsville, Ontario. The Hotel completed its best year since its acquisition in 1988, resulting in a 54% occupancy level, \$0.39 million of operating earnings, and \$0.55 million of operating cash flow. The mid-1992 renovation, completed in conjunction with the Best Western affiliation, together with the early 1993 inauguration of the Golden Griddle franchise, have assisted management in generating steadily improving occupancy levels, cost efficiencies, and bottom line results.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

In 1995, the Company's U.S. subsidiary, The Equion Corporation, began the process of selling its business units. The sales to date include the Signet Systems division together with its Signet AutoAir subsidiary in July 1995 (the "Signet Sale"), the TCI division in December 1995, the Trans-Tool division in February 1996, the Hayden division's engine driveline ("EDL") product line in April 1996, and Hayden's aftermarket cooling business (the "A/M Sale") in December 1996.

In addition during fiscal 1996, Equion repurchased all of the shares held by its minority shareholders for \$12.8 million. In a related transaction with one of those minority shareholders (Equion's former chief executive officer), Enscor repurchased 477,931 of its common shares at \$1.10 Cdn. per share and prepaid a \$0.6 million promissory note. Also in 1996, Enscor redeemed all of its outstanding preferred shares for \$5.0 million.

Following the A/M Sale, for internal corporate planning purposes and to simplify organizational holdings, the Company restructured a number of its subsidiaries. Pursuant to this restructuring, Equion was liquidated into another U.S. subsidiary and Hayden's remaining industrial cooling products business was transferred to a separate wholly-owned entity. This internal restructuring did not impact the Company's financial statements.

Recently, the Company has refocussed on real estate investment. The short-term focus will be on real estate structured financing, sometimes referred to as merchant banking. Transactions may include mezzanine loans, guarantees, a pre-purchase of inventory, or direct equity participation. These short-term high-yield investments are expected to provide a profitable earnings base and, more importantly, may create opportunities for our long-term business focus. The long-term focus will be to invest in certain specialized, income producing and growth real estate assets. Business areas currently under consideration include assisted care adult living centres, self-storage mini-warehouse facilities, and hotels.

In 1993, the Company adopted the U.S. dollar as a basis for reporting results. As well, effective July 31, 1993, the Company changed its fiscal year end from December 31 to July 31. The Company's audited consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles (see note 15 to the Statements for a reconciliation to U.S. generally accepted accounting principles).

Financial Condition, Liquidity, and Capital Resources

The Company's working capital decreased to \$17.4 million at July 31, 1997, \$3.0 million lower than July 31, 1996 levels. The decrease is substantially attributable to the impact of \$3.5 million of long-term loans receivable plus \$1.0 million of capital expenditures, offset partly by the fixed asset proceeds from the A/M Sale.

The Company has no long-term debt. Of the \$2.3 million balance as at July 1996, \$0.2 million was assumed in connection with the A/M Sale. The \$2.1 million remainder pertained to the Whitby, Ontario land development site which was sold in June 1997 (the "Whitby Sale"). Part of the debt had been paid down in November 1996 and the balance retired upon completion of the sale.

In May 1997, the Company initiated a normal course issuer bid through the facilities of The Toronto Stock Exchange. Under the terms of this bid, the Company may purchase a maximum of 1,148,000 Common Shares over the 12 month period ending May 8, 1998 for an aggregate consideration not exceeding \$1,265,000 (Cdn.). The Company's board of directors believes that the acquisition of Common Shares represents a worthwhile investment due to the market's current undervaluation of the shares. Purchases will be funded out of the Company's surplus cash resources. Pursuant to this bid, the Company purchased 72,000 common shares at an average price of \$1.20 (Cdn.) by July 31, 1997. In September 1997, an additional 12,100 common shares were purchased at \$1.15 (Cdn.).

In addition during fiscal 1997, pursuant to the January 1996 termination of Mr. Paul Loulis, a former Equion executive officer, the Company repurchased 20,000 common shares from Mr. Loulis at \$1.01 (Cdn.) per share.

Cash and short-term investments increased to $12.3 million as at July 31, 1997, $1.5 million higher than at July 31, 1996. The increase is substantially attributable to the proceeds from the A/M and Whitby Sales, less $5.4 million invested in loans receivable pursuant to the Company's new direction into the real estate investment business. Restricted cash remains unchanged at $0.5 million. The Company believes that its unrestricted cash position and operating cash flows are sufficient to meet all known cash commitments. However, it is anticipated that additional cash resources will be required to support the expected expansion of its real estate investment business. In that respect, the Company will, during the balance of fiscal 1998, explore its financing options.

Results of Operations

1997 versus 1996

Summary

Revenues for 1997 were $21 million, versus $57 million last year. The decrease is primarily attributable to the Equion operations which have been sold. Operating earnings of $0.1 million were recorded this year, compared with a $5.9 million loss last year. The impact from the disposal of Equion's assets together with other related charges resulted in a net loss of $0.9 million in 1997 versus a $4.2 million loss in 1996.

Automotive and Industrial

Automotive and industrial sales decreased from $51.9 million in 1996 to $13.8 million in 1997 as a result of the disposal of Equion's business units. This year's sales are entirely attributable to Hayden's remaining industrial cooling products business and are approximately 9% higher than the comparable level last year.

In prior years, Hayden Industrial Products was operated as part of the overall Hayden division which also included the "now sold" EDL product line and the aftermarket business. As a result, certain overhead costs and expenses were shared and not directly divisible. Accordingly, other than sales revenue, there was no precise stand-alone history for Hayden Industrial Products until this year. With the completion of the A/M Sale and the decision to retain Hayden Industrial Products, it was recognized that the standard costing process, inventory control, and the computer system all required upgrading. A new computer system was selected and, after months of preparation, implemented on August 1, 1997. The system will significantly enhance the sophistication level of Hayden's reporting and control procedures, and facilitate a more refined costing and pricing approach with customers.

As part of the implementation process, which required a complete review of the standard costing and inventory control procedures, it was determined that Hayden had not been adequately recording its full cost of sales and that a 2% gross margin adjustment was required. This adjustment, totalling $0.3 million, was recorded in the fourth quarter. Management will carefully monitor margins on an ongoing basis.

For the year, net of the adjustment referred to above, a gross margin of 33.3% was achieved, versus 24.9% last year for all operations. Last year's overall margins were negatively impacted by a variety of factors including higher material purchase costs, unusually high warranty and service claims, underabsorbed overheads related to relatively low production levels, and a second quarter provision for certain obsolete inventory.

Selling, general, and administrative expenses were $4.7 million or 34.0% of sales, versus $15.5 million or 29.8% of sales last year. This year's outlays were negatively impacted by Hayden's transition to a stand-alone operation. It is anticipated that, on an ongoing basis, expenditure levels as a percentage of sales will approximate last year's level. Interest income on surplus funds was $0.7 million, versus $1.0 million last year. Most of the surplus funds from this year will be redeployed in the Company's real estate investment business. Divisional earnings of $0.6 million were recorded this year, versus a $1.6 million loss last year.

A $0.7 million loss was recorded in connection with the completion of the A/M Sale. This loss includes $0.4 million previously estimated during the second quarter, plus an additional $0.3 million representing warranty claims, doubtful receivables, and other costs in excess of previous allowances. As well, a $0.2 million charge was recorded for final settlement of a claim in connection with the Signet Sale. Last year, a $4.6 million gain was

generated by the TCI, TransTool, and EDL sales, less a $0.8 million adjustment related to the Signet Sale. Also, a $0.5 million restructuring charge was recorded in connection with the implementation of ongoing changes at Hayden, intended to improve productivity at their manufacturing and distribution facilities.

Real Estate Investment — Financing and Development

Revenues of $0.2 million were recorded on four loans yielding, on average, about 30% per annum. The loans originated during the fourth quarter of 1997 and are all due within the next two years. Project investigation costs of $0.1 million were incurred in connection with all transactions under consideration, resulting in $0.1 million of earnings.

During the year, the Company sold its last Symphony Place condominium suite and its Whitby site for net proceeds of $4.4 million, resulting in earnings of $0.3 million net of carrying costs for the Whitby site prior to its sale. As well, a $0.5 million charge was recorded to reflect a recent unfavourable decision in connection with the Hidden Valley condominium ligitation matter. Although the Company intends to appeal, full provision has been made for the Company's exposure.

In 1996, revenues of $1.7 million and earnings of $0.1 million were generated by the sale of the Markham land development site and two Symphony Place condominium suites. A $3.2 million provision for diminution in asset value was recorded in connection with the Whitby property, resulting in a $3.1 million net loss.

Real Estate Investment — Hotel

Our Best Western Hidden Valley Resort Hotel recorded revenues of $2.0 million and earnings of $0.39 million this year, an increase of 7% and 131%, respectively, over last year's revenues of $1.9 million and earnings of $0.17 million. The revenue increase reflects higher occupancies and room rates. As a result of the stability of the property, the higher revenues produced, for the most part, dollar-for-dollar higher earnings. Together with other savings and efficiencies, year-over-year earnings more than doubled.

Corporate and Other

Net corporate overheads and other outlays of $0.9 million were incurred this year, versus $1.4 million last year. The difference is primarily attributable to the elimination of dividends and interest on the preferred shares and long-term debt which were repaid during fiscal 1996.

Results of Operations

1996 versus 1995

Summary

Revenues for 1996 were $57 million, versus $141 million in 1995. The decrease is primarily attributable to the Equion operations which were sold commencing in July 1995. An operating loss of $5.9 million was recorded, compared with a loss of $3.6 million in 1995. After including the gain on disposal of the Equion assets together with other related charges, a net loss of $4.2 million was incurred in 1996, versus $8.9 million of net earnings in the previous year.

Automotive and Industrial

Automotive and industrial sales decreased from $139 million in 1995 to $52 million in 1996. The decrease is attributable to Equion's sales of its business units. Excluding the operations which have been sold, there was a 9% increase on a comparable year-over-year basis. This increase was primarily attributable to new customers and additional products at Hayden.

A gross margin of 24.9% was achieved, compared to 25.1% in the prior year (28.0% for the comparable remaining operations). Margins in 1995 were impacted by a provision of $0.5 million (approximately 1.0 percentage point of gross margin) for certain obsolete inventory categories at both Hayden and Trans-Tool. Margins were also affected by higher raw material costs, product returns, unabsorbed overheads resulting from relatively low production levels during the first half of the year, and a less favourable sales mix.

Comparable year-over-year selling, general, and administrative ("SG&A") costs at the divisional level were up by approximately 4% due to higher incentives for existing customers, higher marketing and promotional costs for new customers, and the generally higher sales level in 1996. As a percentage of sales, SG&A costs for the comparable remaining operations increased only modestly to 29.8% in 1996, versus 29.6% in the previous year. The increase resulted, in part, from the higher divisional expenses referred to above. As well, actual corporate expenditures only began to decrease significantly following the January 31, 1996 closing of the Kentucky corporate office. Accordingly, the relatively high full year corporate expenditure level further increased the percentage of sales calculation.

Net interest income of $1.0 million was earned in 1996 on the surplus funds generated by the sales of Equion's business units, versus a $3.4 million expense in 1995.

The combination of all of the above resulted in an operating loss of $1.6 million in 1996, versus a $1.9 million operating loss in the previous year.

The 1996 loss was largely offset by a $4.6 million pre-tax and pre-minority interest gain on the sales of Equion's business units, less a $0.8 million adjustment in connection with the July 1995 Signet Sale and a $0.5 million restructuring charge in connection with the implementation of changes at Hayden. These changes were part of an initiative which commenced in 1995, intended to improve productivity at Hayden's manufacturing and distribution facilities. In 1995, a $21.5 million gain was generated by the Signet Sale, partly offset by a $1.7 million restructuring change for the Hayden initiative described above.

Real Estate Investment — Financing and Development

In 1996, two of the Company's three Symphony Place condominium suites were sold, together with the Markham, Ontario land development site. A $0.1 million profit was recorded on sales proceeds of $1.7 million. After providing for a $3.2 million provision for diminution in asset value related to the Whitby site, a $3.1 million loss was incurred.

In 1995, revenues of $0.3 million were generated primarily by the sale of one Symphony Place condominium suite. A $0.1 million loss was recorded, net of a $0.2 million provision for diminution in asset value related to the Whitby site.

Real Estate Investment — Hotel

Year-over-year revenues at our Best Western Hidden Valley Resort Hotel declined by 3% from $2.0 million in 1995 to $1.9 million in 1996, primarily due to lower food and beverage sales resulting from a change in the customer mix. Occupancy levels and room rates were unchanged. Notwithstanding the lower revenues, earnings from operations increased to $168,000 in 1996, versus $52,000 last year. The increase resulted from improved operating efficiencies, cost reductions, and lower interest charges following the October 1995 prepayment of the hotel's mortgage.

Corporate and Other

Net corporate overheads and other outlays of $1.4 million were incurred in 1996, versus $1.6 million in 1995. Excluding certain one-time savings, there was no appreciable difference on a year-over-year basis.

AUDITORS' REPORT

TO THE SHAREHOLDERS OF ENSCOR INC.

We have audited the consolidated balance sheets of Enscor Inc. as at July 31, 1997 and 1996 and the consolidated statements of earnings, retained earnings and cash flows for each of the years in the three year period ended July 31, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at July 31, 1997 and 1996 and the results of its operations and the changes in its financial position for each of the years in the three year period ended July 31, 1997 in accordance with generally accepted accounting principles.

KPMG

Chartered Accountants

North York, Canada
October 8, 1997

Enscor Inc.

CONSOLIDATED BALANCE SHEET

(Expressed in United States thousands of dollars)

	July 31, 1997	1996
Assets		
Current Assets		
Cash and short-term investments (note 16(d))	$12,338	$10,859
Loans receivable (notes 3 and 4)	1,902	—
Trade receivables, less allowance of $266,000 ($500,000 — 1996) (note 4)	2,086	7,232
Amounts receivable (note 5)	2,778	3,825
Inventories (note 6)	1,218	5,945
Prepaid expenses and other current assets	435	708
Advances to and from related companies (note 7)	(19)	1,070
	20,738	29,639
Capital assets (note 8)	3,038	4,743
Long-term portion of loans receivable (notes 3 and 4)	3,478	—
Goodwill	1,275	1,641
Deferred income taxes	300	66
	$28,829	$36,089
Liabilities		
Current Liabilities		
Accounts payable and accrued liabilities	$ 3,377	$ 7,062
Current portion of long-term debt (note 10)	—	2,220
	3,377	9,282
Other liabilities	579	581
Long-term debt, less current portion (note 10)	—	101
Deferred income taxes	—	66
	3,956	10,030
Shareholders' Equity (note 11)		
Common shares		
Authorized: unlimited		
Issued and outstanding: 22,875,900 — (22,967,907 — 1996)	23,974	24,065
Cumulative translation adjustment	(44)	146
Retained earnings	943	1,848
	24,873	26,059
	$28,829	$36,089

Commitments and contingencies (note 21)

(See accompanying notes)

APPROVED BY THE BOARD

SAM REISMAN
Director

STEPHEN R. MORRISON
Director

Enscor Inc.

CONSOLIDATED STATEMENT OF EARNINGS

(Expressed in United States thousands of dollars
except per common share amounts)

	Year Ended July 31,		
	1997	1996 (Restated note 1)	1995 (Restated note 1)
Net sales	$18,231	$53,615	$138,902
Interest and other income	3,100	3,209	2,164
	21,331	56,824	141,066
Cost of sales	13,054	40,600	104,030
Selling, general, and administrative (notes 16(a) and 17(b))	7,663	17,537	37,404
Depreciation and amortization (note 16(b))	543	1,032	2,565
Provision for diminution in asset values (notes 6 and 14)	—	3,165	203
Dividends paid on preferred shares	—	412	442
	21,260	62,746	144,644
Earnings (loss) from operations	71	(5,922)	(3,578)
Gain (loss) on disposal of assets (note 2)	(919)	3,749	21,541
Restructuring costs (note 9)	—	(500)	(1,726)
Earnings (loss) before income taxes and minority interest	(848)	(2,673)	16,237
Income taxes (recovery) (note 12)			
Current	364	597	2,188
Deferred	(300)	—	(174)
	64	597	2,014
Earnings (loss) before minority interest	(912)	(3,270)	14,223
Minority interest	—	890	5,320
Net earnings (loss)	$ (912)	$(4,160)	$ 8,903
Net earnings (loss) per common share (note 13)			
Basic	$ (0.04)	$ (0.18)	$ 0.38
Fully diluted	$ (0.04)	$ (0.18)	$ 0.35

(See accompanying notes)

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

(Expressed in United States thousands of dollars)

	Year Ended July 31,		
	1997	1996 (Restated note 1)	1995 (Restated note 1)
Balance — beginning of year	$ 1,848	$ 6,085	$(2,818)
Net earnings (loss)	(912)	(4,160)	8,903
Discount on repurchase of common shares	7	—	—
Premium on redemption of preferred shares	—	(77)	—
Balance — end of year	$ 943	$ 1,848	$ 6,085

(See accompanying notes)

Enscor Inc.

CONSOLIDATED STATEMENT OF CASH FLOWS

(Expressed in United States thousands of dollars)

	Year Ended July 31, 1997	1996 (Restated note 1)	1995 (Restated note 1)
Operating activities			
Net earnings (loss)	$ (912)	$(4,160)	$ 8,903
Add (deduct) items not involving cash:			
Loss (gain) on disposal of assets (note 2)	919	(3,749)	(21,541)
Depreciation and amortization	812	1,806	4,463
Minority interest, including dividends paid	—	890	5,518
Provision for diminution in asset values	—	3,165	203
Deferred income taxes	(300)	—	(174)
	519	(2,048)	(2,628)
Changes in non-cash operating balances (note 19(a))	3,809	(1,408)	(6,924)
Cash provided (used) by operating activities	4,328	(3,456)	(9,552)
Financing activities			
Repayment of long-term debt	(2,147)	(4,184)	(27,574)
Loans receivable	(5,424)	—	—
Notes and other receivables	190	3,410	(6,971)
Repurchase of common shares	(91)	(413)	—
Redemption of preferred shares (note 7(b))	—	(4,973)	—
Cash used by financing activities	(7,472)	(6,160)	(34,545)
Investing activities			
Acquisition and development of land and housing	(15)	(612)	(719)
Recovery of costs through sales	2,018	1,624	150
Purchase of capital assets	(991)	(640)	(2,708)
Proceeds on disposal of assets	3,759	22,218	55,008
Cost of acquisitions, net of cash (note 2)	—	(12,756)	(1,461)
Cash provided by investing activities	4,771	9,834	50,270
Effect of exchange rate changes	(148)	13	50
Increase in cash and cash equivalents	1,479	231	6,223
Cash and cash equivalents — beginning of year	10,859	10,628	4,405
Cash and cash equivalents — end of year (note 16(d))	$12,338	$10,859	$10,628

(See accompanying notes)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JULY 31, 1997

(Tabular amounts expressed in United States thousands of dollars, except per common share amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Company are prepared in accordance with accounting principles generally accepted in Canada which conform in all material respects with accounting principles generally accepted in the United States, except as indicated in Note 15.

Principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, together with the Company's proportionate share of the assets, liabilities, revenues and expenses in a partnership and joint ventures. All material intercompany accounts and transactions have been eliminated.

The principal operating business currently included in the consolidated group is Hayden Industrial Products LLC ("Hayden"). Previously, it was The Equion Corporation ("Equion"). For internal corporate planning purposes and to simplify organizational holdings, the Company has restructured a number of its subsidiaries. Pursuant to this restructuring, Equion was liquidated into another U.S. subsidiary effective December 1996, and Hayden's industrial cooling product business has been transferred to a separate wholly-owned entity. This internal restructuring has had no impact on the Company's financial statements.

Basis of presentation

In recognition of substantially all current revenues originating in the United States through Hayden (and previously Equion), the Company reports its results in U.S. dollars. The Company's Canadian operations are translated into United States dollars using the end of period exchange rate for assets and liabilities and an average prevailing rate during the period for revenues and expenses. Any resulting translation gain or loss is recorded in shareholders' equity.

Inventories

Hayden inventories are stated at the lower of cost (first-in, first-out method) and market.

Capitalization of costs — Land and housing under development

The Company follows the policy of capitalizing direct carrying costs such as interest, realty taxes and other related costs to land under development and housing under construction.

The Company also capitalizes that portion of interest on general borrowings considered applicable to land under development and housing under construction.

Land and housing under development is recorded at the lower of cost and estimated net realizable value.

Automotive part sales and warranties

The Company provides 12 — 36 month warranties on certain automotive parts. A warranty accrual is recorded at the time of sale for estimated claims based on historical claims experiences.

Revenue recognition

Revenues from real estate transactions are recognized as follows:

House sales:	at the date when title passes and closing has occurred and all material conditions precedent to closing have been fulfilled or provided for.
Condominium sales:	when the amount due on occupancy is received and the purchaser is entitled to occupancy and undertakes to assume a mortgage for the balance of the purchase price.
Land sales:	when all material conditions precedent to closing have been fulfilled, at least 25% of the purchase price has been received and interest will accumulate at a reasonable rate on the balance which is not subordinated to additional loans on the property.

The Company does not have any continuing involvement with properties sold that would result in retention of any substantial risks or rewards of ownership.

Revenues from real estate investment transactions are recognized as follows:

Loan fees:	fees relating to loan obligations, which are considered an integral part of the yield earned on the loan, are amortized over the term of the loan.

Capital assets

Capital assets are recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives:

Furniture, Machinery and Equipment	five to eight years
Buildings	twenty-eight to forty years
Leasehold Improvements	over the term of the specific leases

Goodwill

Goodwill, the excess of the cost of business acquisitions over the fair value of the underlying assets acquired, is capitalized and amortized on a straight-line basis over thirty years. The Company periodically reviews the carrying value of its goodwill to determine whether an impairment in such goodwill has occurred. Substantially all of the Company's recorded goodwill pertains to its investment in Hayden. Therefore, in its review, the Company considers management's long-term projections of Hayden's operating results, as measured by earnings before interest and taxes, and management's judgment as to the fair value of its investment in Hayden, using objective third-party criteria wherever possible.

Deferred income taxes

The Company follows the deferral method of tax allocation under which income taxes are provided for in the period during which transactions are included in accounting income.

Accounting Change

In 1997, the Company retroactively applied the recommendations set forth in CICA Handbook Section 3860 for financial instruments. Accordingly, certain preferred shares redeemed in 1996 were required to be treated as financial liabilities. The results of operations and changes in financial position have been restated to present the preferred share dividends paid of $412,000 in 1996 and $442,000 in 1995 as an expense.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

2. ACQUISITIONS AND DIVESTITURES

(a) Certain Assets Of Automatic Flywheel, Inc.

On April 19, 1994, Equion acquired the flywheel, ring gear, and cable product lines of Automatic Flywheel, Inc. of Dallas, Texas. The acquired operations were integrated into Equion's Hayden division. The purchase price was $2,039,000, satisfied by a cash payment of $1,829,000 and the assumption of a note payable of $210,000.

(b) Signet AutoAir Klimaanlagen GmbH ("SAA")

On September 1, 1994, Equion acquired, for $1.9 million, an 80% interest in SAA which purchased certain assets of AutoAir Klimaanlagen GmbH. SAA, located in Goch, Germany, is a designer and manufacturer of air-conditioning kits and components serving the automotive, truck, and off-highway vehicular marketplace, primarily in Europe.

(c) Sale of Signet Systems, Inc. ("SSI") and Capital Stock of SAA

On July 31, 1995, Equion completed the sale of all of the business and substantially all of the property, rights, and net assets of SSI, one of its divisions, and all of its capital stock of SAA, for approximately $56.0 million. A $21.5 million pre-tax gain was recorded at the time. Equion received a cash payment of $49.0 million and two promissory notes each for $2.5 million (note 5(a)). As well, an additional $2.0 million of proceeds were receivable under price adjustment provisions of the agreement. SSI's and SAA's net sales for the year ended July 31, 1995, were $76,103,000.

(d) Sale of TCI and Trans-Tool divisions and Engine Driveline product line ("EDL")

Effective December 29, 1995, Equion completed the sale of the business and assets of its TCI division. On February 29, 1996, its Trans-Tool division was sold and, on April 30, 1996, the EDL sale was completed. In total, a $4.6 million pre-tax gain was recorded on proceeds of $23.5 million. This pre-tax gain was offset by a $0.8 million charge representing certain price adjustments in connection with the 1995 sale of SSI and SAA. Combined net sales for TCI, Trans-Tool, and EDL for the year ended July 31, 1996 were $20,971,000 (1995 - $32,362,000).

(e) The Equion Corporation

During fiscal 1996, the Company acquired all of the common shares previously held by the minority shareholders. As a result, Equion became wholly owned by the Company. The total consideration paid for the minority shareholders' 30% interest was $12.8 million.

(f) Sale of the Aftermarket Cooling Business (the "A/M Sales")

In August 1996, Equion completed the first of a two-stage sale of its aftermarket cooling business. The second stage closed in December 1996. A $0.7 million pre-tax loss has been recorded. In addition, a $0.2 million charge has been recorded in settlement of certain outstanding matters pertaining to the 1995 sale of SSI and SAA.

3. LOANS RECEIVABLE

At July 31, 1997, there were four loans receivable, denominated in Canadian dollars, relating to the Company's real estate investment business, totalling $5.4 million ($7.4 million Cdn.) and ranging in amounts between $0.8 million and $2.2 million. The loans earn fees and interest and are expected to yield an average rate of return of about 30%. The loans will be repaid within the next 23 months as follows: $1.9 million by July 31, 1998, and $3.5 million by June 30, 1999. The loans are secured by specific real estate, personal guarantees and general security agreements.

4. CONCENTRATION OF CREDIT RISK

Financial instruments which potentially subject the Company to concentration of credit risk consist principally of trade receivables and loans receivable.

The Company sells to U.S. industrial and vehicular customers. The Company's exposure to credit risk associated with the non-performance of these customers in fulfilling their contractual obligations can be directly impacted by a decline in economic conditions which could impair the customers' ability to satisfy their obligations to the Company. In order to reduce the risks, the Company has credit procedures in place whereby analysis is performed to control the granting of credit to high-risk customers.

The loans receivable are primarily to companies in the real estate development market. The ability of the debtors to meet contractual obligations would be similarly affected by changing economic, political, or other conditions. In order to reduce risks, the Company has credit procedures in place, performs due diligence, and analyzes related financial information on an ongoing basis.

5. AMOUNTS RECEIVABLE

	July 31, 1997 Amount	Interest Rate	July 31, 1996 Amount
Note receivable (a)	$2,379	8.75%	$2,500
Amount due on disposal of assets (b)	—		217
Income taxes receivable	399		650
Other	—		458
	$2,778		$3,825

(a) The note receivable resulted from the sale of SSI and SAA (note 2(c)). The remaining balance was received in September 1997.

(b) This amount represents the balance of proceeds in connection with the EDL sale (note 2(d)).

6. INVENTORIES

	July 31, 1997	July 31, 1996
Automotive and industrial		
Raw materials	$ 731	$2,655
Work in process	351	319
Finished goods	189	1,175
	1,271	4,149
Obsolescence reserve	(53)	(227)
	1,218	3,922
Land and housing under development		
Land		
Acquisition costs	—	3,211
Carrying costs	—	1,572
Development costs	—	910
	—	5,693
Housing	—	193
	—	5,886
Provision for diminution	—	(3,863)
	—	2,023
	$1,218	$5,945

7. RELATED PARTY TRANSACTIONS

(a) Advances to and from related companies are non-interest bearing, have no specific terms of repayment, and consist of the following:

	July 31, 1997	July 31, 1996
Advances to	$ —	$1,479
Advances from	19	409
	$(19)	$1,070

(b) Substantially all of the Company's preferred shares were held by companies which are subsidiaries of a company controlled by a trust for the children of the Company's Chairman. The balance of the preferred shares were held by a company over which control or direction may be exercised by the Company's President. All of the preferred shares were redeemed during fiscal 1996.

(c) $nil ($0.1 million — 1995) of promissory notes were payable to a company that is a subsidiary of a company controlled by a trust for the children of the Company's Chairman. The Company's Chairman is the President and a director of that company. This debt was secured by mortgages receivable. In addition $nil ($0.9 million — 1995) of promissory notes were payable to a former director of the Company and were secured by a pledge of a portion of the Company's shares in Equion. All of the above promissory notes were repaid during the 1996 fiscal year.

(d)

	Year Ended July 31, 1997	1996	1995
Fees paid for management and other services provided*	$889	$1,204	$1,011
Interest paid on the promissory notes referred to in note 7(c)	$ —	$ 72	$ 107

* by the company referred to in note 7(c) together with one of its subsidiaries, and by a former director of the Company.

(e) The Company leases approximately 17,500 square feet of office space in Don Mills, Ontario from a corporation controlled by a person related to the Company's Chairman, for $162,000 annually. The lease was renewed and now expires in 2002. The Company subleases part of the office space to the company referred to in note 7(c) for $62,000 annually.

8. CAPITAL ASSETS

	Cost		Accumulated depreciation and amortization		Net Book Value	
	July 31, 1997	July 31, 1996	July 31, 1997	July 31, 1996	July 31, 1997	July 31, 1996
Hotel land	$1,183	$ 1,186	$1,114	$1,117	$ 69	$ 69
Hotel building and equipment	3,706	3,670	2,650	2,500	1,056	1,170
Furniture, equipment, and leasehold improvements	1,736	2,011	1,147	1,413	589	598
Automotive machinery and equipment	1,527	4,596	203	1,690	1,324	2,906
	$8,152	$11,463	$5,114	$6,720	$3,038	$4,743

Accumulated depreciation and amortization includes a $1,967,000 provision for decline in value of the hotel assets.

9. RESTRUCTURING AND OTHER CHARGES

Restructuring charges of $1,726,000 for 1995 included the following costs relating to the relocation of Hayden's automotive parts distribution facility from California to Tennessee and the planned closure of the Company's corporate office in Kentucky by January 1996 as a result of the sale of SSI: (i) $889,000 for termination benefits for eight California and Kentucky employees, (ii) $737,000 to relocate the distribution facility to Tennessee, and (iii) $100,000 to close the Kentucky corporate office. Of these total costs, $401,000 were paid in 1995 towards relocating the distribution facility and the unpaid balance of $1,325,000 was included in accounts payable and accrued liabilities as at July 31, 1995.

In January 1996, an additional charge of $500,000 for termination benefits was recorded to reflect revised estimates for the Hayden restructuring. In 1996, $1,518,000 of the above restructuring charges were paid and the balance of $307,000 was included in accounts payable and accrued liabilities. That balance was paid during the 1997 fiscal year.

10. LONG-TERM DEBT

	July 31,	
	1997	1996
Mortgage payable	$ —	$2,121
Notes payable	—	200
	—	2,321
Less: current portion	—	2,220
	$ —	$ 101
Weighted average interest rates	—	8.3%

11. SHAREHOLDERS' EQUITY

(a) Changes in the Company's outstanding common share capital were as follows:

	Number of Shares		Amount	
	July 31, 1997	July 31, 1996	July 31, 1997	July 31, 1996
Balance — beginning of year	22,967,907	23,445,846	$24,065	$24,478
Shares repurchased	(92,000)	(477,931)	(91)	(413)
Fractional shares eliminated pursuant to a prior acquisition	(7)	(8)	—	—
Balance — end of year	22,875,900	22,967,907	$23,974	$24,065

The aggregate legal stated capital of the common shares of the Company is $13.2 million.

(b) The following stock option plan was in effect in 1997:

1985 Stock Option Plan —

Options have been granted to certain employees under this Plan which vest over five years and expire on the earlier of 10 years from the date of grant or on termination of employment, unless otherwise stated. Total options under the Plan are limited to 643,100. During 1997, no options were granted or expired, leaving 80,000 fully exerciseable options outstanding at prices ranging from $1.53 U.S. to $2.60 Cdn.

12. INCOME TAX INFORMATION

(a) Income Taxes

Income taxes including current and deferred portions, have been computed as follows:

	Year Ended July 31,		
	1997	1996	1995
Combined Canadian federal and provincial income tax rate	44.6%	44.3%	44.3%
Earnings (loss) before income taxes and minority interest	$ (848)	$(2,673)	$16,237
Items which are non-deductible:			
Permanent differences	1,419	5,166	9,633
Losses not tax effected	928	4,058	1,207
	$1,499	$ 6,551	$27,077
Tax at basic rates	$ 669	$ 2,902	$11,995
Decrease in taxes resulting from:			
Effects of United States operations	(29)	(367)	(1,536)
Realization of benefits of loss and depletion carryforwards	(597)	(1,952)	(8,485)
	43	583	1,974
Federal capital tax	21	14	40
Income taxes	$ 64	$ 597	$ 2,014
Effective tax rate	(7.5)%	(22.3)%	12.4%

(b) Substantially all of the components of the Company's income before income tax expense are derived from the Company's United States operations.

(c) At July 31, 1997, the Company and its subsidiaries had operating loss carryforwards for Canadian tax purposes which expire as follows:

July 31	
1998	$ —
1999	24
2000	566
2001	2,490
2002	1,046
2003 and after	5,108
	$9,234

The future tax benefits of these operating losses have not been recognized for financial reporting purposes.

(d) Deferred tax assets of $300,000 at July 31, 1997 resulted from the excess of the tax basis of capital assets and goodwill over their book basis.

13. NET EARNINGS (LOSS) PER COMMON SHARE

The weighted average number of outstanding shares which was used to calculate net earnings (loss) per common shares was:

	Year Ended July 31,		
	1997	1996	1995
Basic	22,950,107	23,363,571	23,445,846
Fully diluted	23,030,107	26,635,588	26,885,398

14. INVESTMENT IN REAL ESTATE PARTNERSHIP AND JOINT VENTURES

Included in the consolidated financial statements are the accounts of the following:

	Participation Interest
Rose Homes Partnership (included in the Rose Homes Partnership is a 50% interest in the Rosedale North Joint Venture)	98%
Whitby Joint Venture	75%

The proportionate share of, or undivided interest in, the above assets, liabilities, revenues, and expenses is reflected in the consolidated financial statements as follows:

	Year Ended July 31,		
	1997	1996	1995
Assets	$ 1	$5,099	$7,194
Liabilities	1	2,136	2,184
Revenues	4,243	—	4
Cost of sales	3,658	—	—
Expenses	280	—	—
Provision for diminution	—	3,165	—

The assets and liabilities shown above are primarily those of the Whitby Joint Venture. The revenues, cost of sales, expenses and provision for diminution for the years ended July 31, 1997 and 1996 relate specifically to the Whitby Joint Venture.

15. SIGNIFICANT DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian Basis") which differ in certain respects from those prepared in accordance with accounting principles and practices generally accepted in the United States ("U.S. Basis"). Under the U.S. Basis certain items in the Consolidated Statement of Earnings and the Consolidated Balance Sheet would have been reported as follows:

(a) Consolidated Statement of Earnings

	Year Ended July 31, 1997	1996	1995
Net earnings (loss) — Canadian Basis	$ (912)	$(4,160)	$ 8,903
Increased depreciation and amortization (i)	32 (45)	(154)	(548)
Increased selling, general, and administrative expenses (iii)	—	—	(344)
Decreased (increased) tax provision — deferred (i) (ii)	8 (204)	(425)	(61)
Decreased gain on disposal of assets (i) (ii) (iii)	36 (378)	(1,027)	(3,104)
Add back dividends paid on preferred shares (iv)	—	412	442
Net earnings (loss) — U.S. Basis	$(1,539)	$(5,354)	$ 5,288
— per common share	$ (0.07)	$ (0.25)	$ 0.21

(b) Consolidated Balance Sheet

S/E rec.
96 97.
79 <45> = 34
218 <204> = 14
526 <378> = 148
Total 196

	July 31, 1997 Canadian Basis	July 31, 1997 U.S. Basis	July 31, 1996 Canadian Basis	July 31, 1996 U.S. Basis
Assets				
Capital assets (net) (i)	$ 3,038	$3,038	$ 4,743	$5,276
Goodwill (i)	1,275	1,275	1,641	1,928
Deferred income taxes — asset (ii)	300	496	66	909
Liabilities and shareholders' equity				
Deferred income taxes — liability (i)	—	—	66	906
Retained earnings	943	1,139	1,848	2,671

196

(i) Under the Canadian Basis, the fair values of the net assets acquired in a business combination are adjusted for differences from the amounts that will be used for tax purposes, whereas under the U.S. Basis deferred income taxes are recorded on such differences. With the completion of the A/M Sale, there are no remaining differences between the U.S. Basis and the Canadian Basis for capital assets, goodwill and deferred income taxes payable.

(ii) Under the Canadian Basis, the tax benefit of certain operating loss carryforwards of an acquired company were not recognized as an asset at the date of acquisition because there was no reasonable assurance of realization of such benefits. The tax benefits of these loss carryforwards are recognized as a reduction of income tax expense only when they are realized. Under the U.S. Basis, as set forth in Statement of Financial Accounting Standards ("FAS") No. 109, the tax benefits may be recognized in a subsequent year when a change in circumstances justifies a decrease in the related valuation allowance. These benefits are first applied to reduce to zero any goodwill related to the acquisition, next applied to reduce to zero any intangible assets related to the acquisition and finally applied to reduce income tax expense. As at July 31, 1997 and 1996, management continued to recognize deferred tax assets on the basis that reversing taxable temporary differences and estimates of taxable income for the succeeding two years indicated that realization of the assets was more likely than not.

(iii) Under the Canadian Basis, current costs of postretirement health care and life insurance benefits for certain SSI employees were expensed on a cash basis. Under the U.S. Basis, these benefits were accounted for in accordance with the provisions of FAS 106, which requires accrual, during the period of employment, of the expected cost of providing the benefits to the employees.

The following is an analysis of the amounts included in the U.S. Basis measurements:

	Year Ended July 31, 1995
Current service cost	$ 214
Interest on unfunded liability	548
Amortization of unrecognized losses	99
Less cash expenses under Canadian Basis	(370)
	$ 491
U.S. Basis adjustment at 69.95%	$ 344

Prior to the sale of SSI, Equion's Board of Directors adopted amendments to SSI's retiree medical and life insurance plans that reduced its accumulated postretirement benefit obligation by approximately $2.5 million. The proportionate effect of this plan amendment has been included in the Company's gain on sale of SSI.

(iv) Under the U.S. Basis, dividends paid on preferred shares would not be included in the determination of net earnings.

(c) *Primary Earnings Per Share*

The Company's outstanding stock options are considered to be common stock equivalents for the purpose of determining primary earnings per common share. They are excluded, however, from the determination to the extent that they are anti-dilutive. Primary earnings (loss) per common share are $(0.04) ($(0.18) — 1996; $0.38 — 1995).

(d) *Joint Ventures*

Under the U.S. Basis, joint ventures would be accounted for on an equity or consolidated basis, as appropriate. The use of these methods would not result in any differences to net earnings or shareholders' equity.

(e) *Statement of Cash Flows*

Under the U.S. Basis, the cash received in 1996 on notes and other receivables of $3.4 million would be added to proceeds of disposal of $22.2 million and, in 1995, the amounts receivable of $7.0 million from the disposal of assets would be netted against the proceeds of disposal of $55.0 million. Also, under the U.S. Basis, the restricted cash indicated in note 16(d) would be excluded from cash and cash equivalents.

(f) *FAS 121*

"Accounting for the impairment of long-lived assets and for long-lived assets to be disposed"

The 1997 fiscal year is the initial year of application of FAS 121 "Accounting for the impairment of long-lived assets and for long-lived assets to be disposed". If FAS 121 had been applied as at July 31, 1996 and 1995, there would have been no material effect on the Company's financial position or results of operations.

16. OTHER INFORMATION

(a) Research and Development

Included in selling, general, and administrative expenses are approximately $21,000 ($76,000 — 1996; $4,171,000 — 1995) of research and development costs.

(b) Depreciation and Amortization

Total depreciation and amortization expense is $812,000 ($1,806,000 — 1996; $4,463,000 — 1995) of which $269,000 ($774,000 — 1996; $1,898,000 — 1995) is included in cost of sales and $nil ($nil — 1996; $450,000 — 1995) represents amortization of deferred financing fees.

(c) Sales to Major Customers

There were no major customers for the years ended July 31, 1997 and July 31, 1996. Sales to each of two major customers in the automotive and industrial segment for the year ended July 31, 1995 were $33,731,000 and $14,983,000 respectively.

(d) Cash and Short-Term Investments

$495,000 ($538,000 — 1996) of cash and/or short-term investments are being held to secure outstanding letters of credit in connection with the real estate development operations. The cash and short-term investments include $10,691,000 denominated in Canadian dollars.

(e) Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities include accrued liabilities in the amount of $824,000.

17. INTEREST ALLOCATION

(a) Capitalized interest is charged to the cost of sales of land on a proportionate basis of units sold to total units for each project. Interest incurred and charged to cost of sales is summarized below:

	Year Ended July 31,		
	1997	**1996**	**1995**
Interest capitalized — beginning of year	$ —	$670	$457
Interest incurred	—	195	213
		865	670
Interest expensed	—	(865)	—
Interest capitalized — end of year	$ —	$ —	$670

(b) Interest Expense

Selling, general and administrative expenses include interest of $nil ($248,000 — 1996; $3,751,000 — 1995).

18. SEGMENTED INFORMATION

The following summarizes the Company's operations by industry segment:

	Automotive and Industrial (1)	Real Estate Investment: Financing and Development	Real Estate Investment: Hotel	Corporate and Other	Total
July 31, 1997					
Revenues	$ 14,501	$ 4,675	$ 2,022	$ 133	$ 21,331
Cost of sales and expenses	13,888	4,733	1,633	1,006	21,260
Earnings (loss) from operations	$ 613	$ (58)	$ 389	$ (873)	$ 71
Total assets	$ 11,333	$ 5,936	$ 1,525	$10,035	$ 28,829
Depreciation and amortization	$ 646	$ —	$ 162	$ 4	$ 812
July 31, 1996					
Revenues	$ 52,929	$ 1,745	$ 1,893	$ 257	$ 56,824
Cost of sales and expenses	54,498	4,818	1,725	1,705	62,746
Earnings (loss) from operations	$ (1,569)	$(3,073)	$ 168	$(1,448)	$ (5,922)
Total assets	$ 29,992	$ 4,076	$ 1,587	$ 434	$ 36,089
Depreciation and amortization	$ 1,576	$ —	$ 156	$ 74	$ 1,806
July 31, 1995					
Revenues	$138,709	$ 252	$ 1,960	$ 145	$141,066
Cost of sales and expenses	140,639	331	1,908	1,766	144,644
Earnings (loss) from operations	$ (1,930)	$ (79)	$ 52	$(1,621)	$ (3,578)
Total assets	$ 61,575	$ 8,116	$ 1,651	$ 1,268	$ 72,610
Depreciation and amortization	$ 4,203	$ —	$ 157	$ 103	$ 4,463

(1) The Company's automotive and industrial operations are located primarily in the United States.

19. ADDITIONAL INFORMATION

(a) Details of net changes in non-cash operating balances as reported in the Consolidated Statement of Cash Flows are as follows:

	Year Ended July 31, 1997	1996	1995
Trade receivables	$ 5,146	$ 3,731	$ (1,895)
Amounts receivable	859	221	391
Inventories (automotive)	160	2,817	(6,917)
Advances to and from related companies	1,095	(176)	(133)
Accounts payable and accrued liabilities	(3,529)	(6,167)	2,420
Prepaid expenses and other assets	82	468	(619)
Income taxes payable	—	(1,800)	1,643
Other liabilities	(4)	(502)	(1,814)
	$ 3,809	$ (1,408)	$ (6,924)

(b) Cash paid for income taxes and for interest (net of amount capitalized) is as follows:

	Year Ended July 31,		
	1997	1996	1995
Income taxes	$ 118	$ 3,004	$ 581
Interest (net of amount capitalized)	$ 187	$ 266	$ 3,902

20. EMPLOYEE BENEFIT PLANS

Equion maintained a noncontributory defined benefit pension plan covering substantially all employees. The plan provided pension benefits based on the employee's years of service and compensation. In all cases, funding was limited to amounts deductible for tax purposes and was at least equal to the minimum contribution required by law. The projected unit credit actuarial method was used to determine pension cost for financial accounting purposes. In May 1997, the plan was frozen and the defined contribution plan (see below) was enhanced.

Net periodic pension cost (income) includes the following components:

	Year Ended July 31,		
	1997	1996	1995
Service cost — benefits earned during the year	$ 86	$ 156	$ 367
Interest cost on projected benefit obligation	131	143	345
Actual return on assets	(86)	(116)	(533)
Net amortization and deferral	(57)	(13)	271
Curtailment gain, net of minimum liability adjustment of $170,000	(198)	—	—
	$(124)	$ 170	$ 450

Assumptions used in accounting for the plan were primarily as follows:

	Year Ended July 31,		
	1997	1996	1995
Discount rate	6.65%	7.75%	7.75%
Rate of increase in compensation level	N/A	4.0%	4.0%
Expected long-term rate of return on assets	9.0%	9.0%	8.0%

The following table sets forth the plan's funded status and amounts recognized in the Company's Consolidated Balance Sheet:

	July 31,		
	1997	1996	1995
Actuarial present value of benefit obligations:			
Vested benefit obligation	$2,004	$1,382	$1,198
Accumulated benefit obligation	$2,004	$1,480	$1,280
Projected benefit obligation	$2,004	$1,783	$1,629
Plan assets at fair value	(1,588)	(1,467)	(1,257)
Projected benefit obligation in excess of plan assets	416	316	372
Unrecognized net gain	—	364	346
Pension liability in the balance sheet	$ 416	$ 680	$ 718

The defined benefit plan's assets are invested in money market accounts and U.S. Treasury bonds with an investment management company.

Hayden also sponsors a defined contribution and deferred compensation plan covering substantially all employees. Contributions are determined based on various methodologies including matching a certain

percentage of each participating employee's contribution and contributing a specified percentage of covered employees' annual base compensation each year. In addition, the employees may share in year end profit-sharing distributions. The Company's expense for these plans approximated $83,000 ($252,000 — 1996; $1,152,000 — 1995).

21. COMMITMENTS AND CONTINGENCIES

(a) Minimum annual payments under the following commitments are:

Years ending July 31	Leased Premises	Management and Other Services	Total
1998	$ 281	$369	$ 650
1999	312	—	312
2000	312	—	312
2001	312	—	312
2002	312	—	312
	$1,529	$369	$1,898

Under the leases, the Company is responsible for taxes, insurance, and maintenance, no portion of which is set out in this note, and sub-leases part of its Canadian office space to one party for $62,000 annually (note 7(e)), and one other party for $38,000 annually. The fees commitment for management and other services expires on December 31, 1997, and will be reviewed at that time (note 7(d)).

(b) Letters of credit have been issued with respect to two land and housing development projects totalling $0.5 million at July 31, 1997 ($0.5 million — 1996).

(c) The Company is a defendant in one lawsuit relating to product liability arising from an accident allegedly occurring in connection with the use of certain equipment which was formerly manufactured and/or distributed by Equion. The claimants allege substantial damages. Certain other similar lawsuits have been settled during past years without any significant adverse effect upon Equion. While the outcome of this lawsuit cannot be predicted with certainty, management, after consultation with legal counsel, is of the opinion, based on the facts known to it, that the liability, if any, from this lawsuit (to the extent not provided for by insurance or otherwise) will not have a material adverse effect upon the Company's consolidated financial position or its results of operations or liquidity.

(d) One of the Company's subsidiaries is a defendant, along with others, in a lawsuit alleging damages and deficiencies arising out of construction of the Symphony Place condominium tower. The Company believes that the claim is unlikely to succeed. In any event, exposure is likely limited to defence costs.

(e) The Company has identified certain environmental matters relating to soil contamination and waste water treatment systems at certain of its U.S. manufacturing facilities. The Company incurred $69,000 ($264,000 — 1996; $395,000 — 1995) of remediation costs during the year. The balance of the liability accrued at July 31, 1997 is $275,000. A final assessment has been prepared by independent consultants and remediation is underway.

22. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

The carrying values of cash and short-term investments, trade receivable, accounts payable and accrued liabilities approximate their fair value due to the relatively short periods to maturity of the instruments.

The fair values of amounts receivable and loans receivable approximate their fair value because they bear interest rates that reflect current rates available to the Company for similar instruments.

23. SUBSEQUENT EVENTS

After year end, the Company committed to provide financing of approximately $4.8 million for three real estate projects in downtown Toronto. The projects are expected to be completed within 30 months.

24. COMPARATIVE FIGURES

Certain prior years' accounts have been reclassified to conform with the current year's presentation.

Enscor Inc.

SELECTED FINANCIAL DATA
(Expressed in United States thousands of dollars except per common share amounts)

	Year Ended July 31,				7 Months Ended July 31,	Year Ended December 31,				
	1997	1996	1995	1994	1993	1992	1991	1990	1989	1988
Revenues	$21,331	$56,824	$141,066	$126,554	$31,464	$29,701	$17,725	$59,138	$37,018	$22,523
Cost of sales and expenses	21,260	59,581	144,441	122,618	30,639	27,262	17,647	53,916	27,369	18,081
Provision for diminution in asset values	—	3,165	203	1,003	829	5,508	1,992	12,754	315	—
Earnings (loss) from operations	71	(5,922)	(3,578)	2,933	(4)	(3,069)	(1,914)	(7,532)	9,334	4,442
Share of income (loss) from investments	—	—	—	(94)	—	(353)	(1,194)	(707)	(648)	92
Gain (loss) on disposal of assets	(919)	3,749	21,541	—	—	—	—	—	—	—
Restructuring costs	—	(500)	(1,726)	—	—	—	—	—	—	—
Earnings (loss) before income taxes and minority interest	(848)	(2,673)	16,237	2,839	(4)	(3,422)	(3,108)	(8,239)	8,686	4,534
Income taxes — current	364	597	2,188	501	429	47	193	(4,296)	3,331	1,232
— deferred	(300)	—	(174)	222	(264)	(1,444)	(1,519)	834	1,062	736
Net earnings (loss) before minority interest	(912)	(3,270)	14,223	2,116	(169)	(2,025)	(1,782)	(4,777)	4,293	2,566
Minority interest	—	890	5,320	1,560	511	—	—	—	—	—
Earnings (loss)	$ (912)	$(4,160)	$ 8,903	$ 556	$ (680)	$(2,025)	$(1,782)	$(4,777)	$ 4,293	$ 2,566
Net earnings (loss) per common share	$ (0.04)	$ (0.18)	$ 0.38	$ 0.02	$ (0.04)	$ (0.12)	$ (0.13)	$ (0.44)	$ 0.39	$ 0.24
Total assets	$28,829	$36,089	$ 72,610	$ 93,635	$90,264	$35,373	$49,085	$69,141	$85,826	$51,224
Long-term debt, including current portion	$ —	$ 2,321	$ 7,005	$ 34,488	$35,094	$11,633	$23,713	$40,962	$36,827	$20,956
Redeemable preferred shares	$ —	$ —	$ 4,896	$ 4,896	$ 4,896	$ 3,400	$ 3,400	$ 2,155	$ 2,155	$ 2,155

See note 2 to the Company's audited consolidated financial statements included herein for a description of certain acquisitions and divestitures made by the Company during the periods presented. See note 15 for a reconciliation of certain of such data to U.S. generally accepted accounting principles.

Enscor Inc.

SUPPLEMENTARY DATA

QUARTERLY FINANCIAL INFORMATION
(Expressed in United States thousands of dollars
except per common share amounts)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
1997					
Net sales	$ 3,049	$ 2,921	$ 3,806	$ 8,455	$ 18,231
Interest and other income	941	508	620	1,031	3,100
Total revenues	$ 3,990	$ 3,429	$ 4,426	$ 9,486	$ 21,331
Gross profit	$ 1,106	$ 984	$ 1,341	$ 1,746	$ 5,177
Earnings (loss) before income taxes and minority interest	$ 85	$ (630)	$ (100)	$ (203)	$ (848)
Net earnings (loss)	$ 38	$ (642)	$ (102)	$ (206)	$ (912)
Net earnings (loss) per common share	$ 0.00	$ (0.03)	$ 0.00	$ (0.01)	$ (0.04)
1996					
Net sales	$15,827	$11,877	$15,421	$10,490	$ 53,615
Interest and other income	908	501	665	1,135	3,209
Total revenues	$16,735	$12,378	$16,086	$11,625	$ 56,824
Gross profit	$ 4,156	$ 1,879	$ 4,051	$ 2,929	$ 13,015
Earnings (loss) before income taxes and minority interest	$ (519)	$(2,381)	$ 1,113	$ (886)	$ (2,673)
Net loss	$ (467)	$(2,826)	$ (295)	$ (572)	$ (4,160)
Net loss per common share	$ (0.02)	$ (0.12)	$ (0.01)	$ (0.03)	$ (0.18)

MARKET FOR THE REGISTRANT'S COMMON SHARES AND RELATED SECURITY HOLDER MATTERS

The Company's Common Shares were offered to the public on April 23, 1981, and thereafter, have been traded on the NASDAQ Over-The-Counter market in the United States. The current NASDAQ symbol is ENCRF. On December 17, 1987, the Company's Common Shares were listed for trading under the symbol ENZ on The Toronto Stock Exchange (Canada).

The high and low bid quotations on The Toronto Stock Exchange reported in Canadian dollars and the NASDAQ Over-The-Counter market reported in United States dollars for each fiscal quarterly period indicated were as follows:

THE TORONTO STOCK EXCHANGE
(expressed in Canadian dollars)

	1997		1996		1995	
	High	Low	High	Low	High	Low
1st Quarter	$1.40	$1.00	$1.55	$1.00	$1.30	$1.15
2nd Quarter	1.30	0.91	1.40	0.90	1.25	1.10
3rd Quarter	1.16	1.10	1.30	1.00	1.75	1.10
4th Quarter	1.40	1.15	1.30	1.00	1.75	1.40

NASDAQ

	1997		1996		1995	
	High	Low	High	Low	High	Low
1st Quarter	$0.94	$0.69	$1.25	$0.69	$0.81	$0.75
2nd Quarter	0.81	0.69	1.06	0.68	0.81	0.75
3rd Quarter	0.83	0.75	1.00	0.68	1.06	0.69
4th Quarter	0.94	0.75	0.94	0.68	1.12	1.00

The NASDAQ Over-The-Counter market quotations reflect inter-dealer prices, without retail mark-up, mark-down, or commission, and may not represent actual transactions.

As of October 1, 1997, there were approximately 1,600 Common shareholders of record. No dividends have been paid on the Common Shares. It is the Company's present policy not to pay cash dividends, but to retain earnings to finance expansion, growth, and investment. Payment of future dividends will be at the discretion of the Board of Directors and will be dependent on the Company's financial condition.

The Investment Canada Act ("ICA") provides that the acquisition of control of a Canadian corporation by a non-Canadian may be subject to review and approval under the ICA, and may be prohibited unless such acquisition is found by the responsible Minister of the Canadian government likely to be of net benefit to Canada.

Dividends paid on Common Shares owned by a non-resident of Canada are subject to Canadian withholding tax under the Income Tax Act (Canada). The general rate of Canadian withholding tax on dividends paid to a non-resident person is 25% of the gross amount of the dividends. This rate may be reduced where there is an applicable tax treaty in existence between Canada and the country of the non-resident dividend recipient.

Under the Canada-U.S. tax treaty, dividends paid by the Corporation to a resident of the United States are generally subject to a Canadian withholding tax of 15% of the gross amount of the dividends.

CORPORATE DIRECTORY

OFFICERS

Sam Reisman
Chairman and
Chief Executive Officer

Stephen R. Morrison
President

Martin Simon
Chief Operating Officer and
Chief Financial Officer

Tim Bankier
Vice President

Ken Ferguson
Vice President

Lana Sherman
Senior Controller

Gary Steinhart
Corporate Secretary

DIRECTORS

Sam Reisman 2, 3
Chairman and
Chief Executive Officer
Enscor Inc.

Peter F. Chodos 1, 3
Executive
Philip Services Corp.

Richard J. Dumler 1, 2
Vice President
Lambda Fund Management Inc.

Seymour Epstein 1
Chairman
Seyton Ltd.,
Video Age Ltd.,
and Imagineering Ltd.

Bryan Levman
President
Guidelines Advertising

Stephen R. Morrison 1, 2, 3
President
Enscor Inc.

Elan Pratzer
Executive
Elan Pratzer & Partners Inc.

FORM 10-K

Shareholders may obtain, without charge, a copy of the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission, by contacting:

Corporate Secretary
Enscor Inc.
156 Duncan Mill Road, Suite 12,
Don Mills, Ontario, Canada
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CORPORATE INFORMATION

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Legal Counsel:	Cassels Brock & Blackwell
Auditors:	KPMG
Transfer Agent:	CIBC Mellon Trust Company
Trading Symbols:	TSE: ENZ NASDAQ: ENCRF

1. Indicates member of Audit Committee
2. Indicates member of Compensation Committee
3. Indicates member of Executive Committee